

Audit Report



ARMY FY 1999 FINANCIAL REPORTING OF CONVENTIONAL AMMUNITION

Report No. D-2000-181

September 1, 2000

Office of the Inspector General
Department of Defense

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Acronym

OM&S

Operating Materials and Supplies



**INSPECTOR GENERAL
DEPARTMENT OF DEFENSE
400 ARMY NAVY DRIVE
ARLINGTON, VIRGINIA 22202-2884**

August 31, 2000

**MEMORANDUM FOR UNDER SECRETARY OF DEFENSE (COMPTROLLER)
AUDITOR GENERAL, DEPARTMENT OF THE ARMY**

**SUBJECT: Audit Report on Army FY 1999 Financial Reporting of Conventional
Ammunition (Report No. D-2000-181)**

We are providing this report for your review and comment. We considered management comments on a draft of this report when preparing the final report.

DoD Directive 7650.3 requires that all recommendations be resolved promptly. Comments from the Deputy Assistant Secretary of the Army (Financial Operations) on the draft of this report were not responsive. Therefore, we request that the Assistant Secretary of the Army (Financial Management and Comptroller) provide additional comments on Recommendations 1. and 3. by October 31, 2000.

We appreciate the courtesies extended to the audit staff. Questions on the audit should be directed to Mr. James L. Kornides at (614) 751-1400, extension 11, e-mail jkornides@dodig.osd.mil, or Mr. John K. Issel at (614) 751-1400, extension 12, e-mail jissel@dodig.osd.mil. See Appendix B for the report distribution. The audit team members are listed inside the back cover.

A handwritten signature in black ink, reading "Robert J. Lieberman", is positioned above the typed name.

Robert J. Lieberman
Assistant Inspector General
for Auditing

Office of the Inspector General, DoD

Report No. D-2000-181

(Project No. D2000FJ-0069.001)

August 31, 2000

Army FY 1999 Financial Reporting of Conventional Ammunition

Executive Summary

Introduction. This report is the first in a series of reports resulting from our audit of the DoD financial reporting of operating materials and supplies. This report discusses the Army reporting of conventional ammunition, which is a material part of the Army operating materials and supplies.

In general, conventional ammunition consists of any item containing explosives. At \$18.9 billion, conventional ammunition, reported as operating materials and supplies, represented 26 percent of the \$72.3 billion in total assets that the Army reported and was the largest tangible asset amount on the balance sheet.

Objectives. The overall objective of our audit was to obtain information on the financial reporting of operating materials and supplies and the appropriateness of policies and regulations governing accounting for operating material and supplies. We focused this part of the audit on the FY 1999 Army financial statements' reporting of conventional ammunition. As part of the audit, we were to assess the internal control structure as it pertained to operating materials and supplies. We did not assess the internal control structure because the Army reported in its FY 1999 financial statements that it lacked the systems and procedures to adequately report operating materials and supplies, including conventional ammunition. This audit was originally announced under Project No. 0FJ-2103.

Results. The FY 1999 Army financial statement reporting for ammunition; as Operating Material and Supplies, needed improvement to meet Federal financial reporting requirements. The Army financial statements could be improved by reflecting the following:

- \$40 billion in adjustments, primarily devaluation of excess, obsolete, and unserviceable ammunition and assets misidentified as missiles;
- \$5 billion of ammunition held overseas as restricted and not for DoD use; and
- a substantial, but unvalued, quantity of chemical munitions held, but prohibited from use by treaty.

The Army reported that it was unable to implement all elements of the Statement of Federal Financial Accounting Standards because of the limitations of its financial management processes and systems, including nonfinancial feeder systems. However, the Army stated that it had been pursuing process and system improvements addressing the limitations of its financial and nonfinancial feeder systems.

Summary of Recommendations. We recommend that the Army reflect in the financial statement footnotes for operating materials and supplies the significant adjustments to the value of operating materials and supplies primarily from devaluation for excess, obsolete, and unserviceable conditions. The Army should remove from "Held in Reserve for Future Use" the dollar value of stock that it owned, but that was not intended for Army use, and reflect the amount under "Restrictions on Operating Materials and Supplies," with an appropriate explanation. Also, the Army should reflect in "Restrictions on Operating Materials and Supplies" the amount of chemical stocks held pending destruction.

Management Comments. The Deputy Assistant Secretary of the Army (Financial Operations) nonconcurred with the recommendations. He stated that the report did not establish a basis for the recommendation to reflect adjustments to logistics data to obtain the values in the financial statements because the information that the auditors recommended be reported was obtained from logistics systems, not the financial statements themselves. He nonconcurred with the recommendation to change the financial reflection of ammunition not intended for Army use and stated that the removal of \$5 billion of Army ammunition that will be used by other nations would cause the Army to understate its assets on the balance sheet. However, he stated that the Army will expand its financial statement notes to include an explanation of usage restrictions for the ammunition. He also nonconcurred with the recommendation to report the quantities of chemical weapons on the financial statements, stating that the reporting was not specifically required by financial guidance. See the Finding section for a summary of management comments and the Management Comments section for the complete text of those comments.

Audit Response. The Deputy Assistant Secretary's responses to the recommendations to reflect the adjustments to the value of operating materials and supplies and to disclose the quantity of chemical stocks are nonresponsive. Financial statements inform decisionmakers in the Department, and Congress, about the value of the assets that DoD has available. Readers of the financial statements should be informed that \$31.6 billion of excess, obsolete, and unserviceable ammunition is on-hand and reported in logistics systems but not included in the amounts presented in the financial statements. Also, the Army should disclose that \$8.4 billion of missiles reported in the logistics systems as ammunition are reported as stewardship assets on the financial statements and that the logistics systems classify \$4 billion of ammunition as missiles. Footnote disclosure of the information is appropriate and essential to explain the difference between the amounts appearing in the financial statements and the amounts shown in the logistics systems. No provision or specific requirement exists to disclose chemical munitions in the financial statements, other than the liability for disposal of them. However, the significance of the existence of 26,200 tons of those stocks, with disposal costs of \$16 billion, merits reporting their existence in the footnotes about Army assets. We request that the Army reconsider its position on these two recommendations in comments to the final report by October 31, 2000.

Although he also nonconcurred with the recommendation to change the reporting of Army ammunition that is not intended for Army use, the Deputy Assistant Secretary proposed expanding the reporting on Army-owned assets that will be used by other nations. The proposed action met the intent of the recommendation.

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Background

Introduction. The audit was performed in support of Public Law 101-576, the "Chief Financial Officers Act of 1990," November 15, 1990, as amended by Public Law 103-356, the "Federal Financial Management Act of 1994," October 13, 1994. This report is part of a series of reports resulting from our audit of the Department of Defense financial reporting of ammunition, as part of operating materials and supplies (OM&S). The audit work was accomplished with the assistance of the Army Audit Agency.

Army Ammunition Financial Reporting. The Army reports OM&S in the Inventory and Related Property, Net, line item of its consolidated balance sheet. Ammunition represented all of the OM&S balance reported on the Army financial statements. The Army reported total assets equal to \$72.3 billion on its balance sheet. At \$18.9 billion, OM&S represented 26 percent of the assets and the largest tangible asset amount on the balance sheet.

The following table shows the categories of OM&S reported in the FY 1999 Army financial statements.

Classes of OM&S Reported by the Army

(dollars in thousands)

<u>Type of OM&S</u>	<u>Value</u>
Held for use	\$ 903,225
Held in reserve for future use	17,996,587
Excess, obsolete, and unserviceable	12,041
Total	\$18,911,853

Army Definitions. This report addresses conventional ammunition only. Conventional ammunition is any item charged with explosives, propellants, pyrotechnics, or chemical material for defense or offense, including demolition. An item of ammunition can range in sophistication from a precision guided missile to a shotgun shell. Conventional ammunition represents all of the OM&S that the Army reported each year in its financial statements.

Army Process and Ammunition System. The Army warehouses ammunition at storage depots, at installations, and on ships and vehicles until the items are issued. The Army Operations Support Command (formerly the Industrial Operations Center), Rock Island, Illinois, is the ammunition inventory manager for the Army and uses the Commodity Command Standard System to monitor the amount and location of ammunition. Other commands also use the system to monitor their assets, which may include ammunition items. The commands are to provide the Army Operations Support Command with information on ammunition for financial reporting purposes. The Commodity Command

Standard System provides information related to the management of materiel and contains cataloging and technical information about each item (for example, national stock number, nomenclature, and net explosive weight).

Objectives

The overall objective of our audit was to obtain information on the financial reporting of OM&S and the appropriateness of policies and regulations governing accounting for OM&S. We focused this part of the audit on the FY 1999 Army financial statements' reporting of conventional ammunition within OM&S. We did not assess the internal control structure because the Army reported in its FY 1999 financial statements that it lacked the systems and procedures to adequately report OM&S. This audit was originally announced under Project No. 0FJ-2103.

Disclosures Needed on Army Financial Reporting of Conventional Ammunition

The FY 1999 Army financial statement reporting for OM&S needed improvement. The Army stated that it was unable to implement all elements of the Statement of Federal Financial Accounting Standards because of the limitations of its financial management processes and systems, including nonfinancial feeder systems. As such, the Army reported, but qualified the appropriateness of, the reported ammunition balance. The Army stated that it had been pursuing process and system improvements and addressing the limitations of its financial and nonfinancial feeder systems.

However, the completeness of the Army financial statements was further impaired because the Army did not disclose other relevant information concerning ammunition reporting, such as the following:

- \$40 billion in adjustments, primarily devaluation of excess, obsolete, and unserviceable ammunition, and assets misidentified as missiles;
- \$5 billion of ammunition held overseas, but not for DoD use; and
- a substantial, but unvalued, quantity of treaty-prohibited chemical munitions held but not intended for use.

Financial Reporting Policy

In Statement of Recommended Accounting Standards No. 3, "Accounting for Inventory and Related Property," October 27, 1993, the Federal Accounting Standards Advisory Board issued accounting principles for OM&S. OM&S are reported as an asset on the balance sheet and were defined as tangible personal property to be consumed in normal operations.

Also, the standard excludes certain asset types from being reported as OM&S:

- goods that have been acquired for use in constructing real property or in assembling equipment for the entity to use,
- stockpile materials,
- goods held under price stabilization programs,
- foreclosed property,

-
- seized and forfeited property, and
 - inventory.

The standard requires OM&S to be categorized as the following:

- OM&S held for use;
- OM&S held in reserve for future use; and
- OM&S excess, obsolete, and unserviceable.

Conventional ammunition that DoD owned and used meets the criteria and is to be reported as OM&S.

For OM&S, the consumption method of accounting is used for the recognition of expenses. The consumption method is an assumption as to when to recognize an expense, in the sense that the eventual use (consumption) results in the recognition in the expenditure account. Under the consumption method, the acquisition of OM&S is viewed as the conversion of resources (from cash to OM&S), not the use of resources. Therefore, the entity still has resources to use. Another method for recognizing OM&S is the purchase method. Under the purchase method, the acquisition of OM&S is considered to be the use of resources; therefore, the entity has used up its resources, that is, expended them.

Also, the standard requires OM&S to be valued on the basis of historical cost. The cost that is recognized when consumed (under the consumption method) would be the past cost of the OM&S item. The first-in/first-out, weighted average, or moving average cost flow assumptions, were the preferred methods for arriving at the historical cost. However, other reasonable valuation methods could be used if the results reasonably approximated the historical cost methods (for example, a standard cost or latest acquisition cost system).

DoD Policy on OM&S. DoD Regulation 7000.14-R, the "DoD Financial Management Regulation," volume 4, "Accounting Policy and Procedures," chapter 4, "Operating Materials and Supplies and Stockpile Materials," updated November 1999, was published to implement the requirements of Standard No. 3 for DoD.

Ammunition Reporting and Disclosure

Even though the Army reported \$18.9 billion under OM&S, all of which was conventional ammunition, in its FY 1999 financial statements, the data contained material financial reporting limitations. In Footnote 1 A, "Significant Accounting Policies: Basis of Presentation," the Army reported that it:

is unable to implement all elements of the SFFAS [Statement of Federal Financial Accounting Standards] due to limitations of its financial management processes and systems, including nonfinancial

feeder systems and processes. Reported values and information for the Army's major asset and liability categories are derived from nonfinancial feeder systems, such as inventory systems and logistics systems. These systems were designed to support reporting requirements focusing on maintaining accountability over assets and reporting the status of federal appropriations and not [the] current emphasis of business-like financial management. As a result, the Army cannot currently implement all elements of the SFFAS. However, the Army continues to implement process and system improvements addressing the limitations to its financial and nonfinancial feeder systems.

Also, under Footnote 1 K, "Inventories and Related Property," which addresses OM&S, the Army reflected two material OM&S reporting limitations. OM&S was limited in the following ways:

- it was valued at standard purchase price, and
- ammunition and munitions not held for sale are treated as OM&S in future years, except in those cases that meet the requirement for the purchase method.

Additionally, under Footnote 8 B, "Operating Materials and Supplies (OM&S), Net," the Army stated the following:

OM&S data, as reported on the financial statements, are derived from logistics systems designed for material management purposes. These systems do not maintain the historical cost data necessary to comply with the valuation requirements of SFFAS No. 3, "Accounting for Inventory and Related Property." In addition, while these logistics systems provide management information on the accountability and visibility over OM&S items, the timeliness at which this information is provided creates issues regarding the completeness and existence of the OM&S quantities used to derive the values reported in the financial statements.

The Army uses the consumption method of accounting for OM&S, where the Army believes it to be more cost beneficial than the purchase method. As stated above, current financial and logistics systems cannot fully support the consumption method. .. However, for FY 1999, significant portions of the Army's OM&S were reported under the purchase method because either the systems could not support the consumption method of accounting or there is a disagreement with the auditing community on what constitutes an item being in the hands of an end user.

Pursuing Improvements

In Footnote 8 B, the Army discussed improvements that it was pursuing in the financial reporting of its OM&S, that is, ammunition. The Army stated the following:

[The Army] has reached an agreement with the Office of Management and Budget; the General Accounting Office; and the Inspector General, Department of Defense, to move to the consumption method of accounting for OM&S in future years. Based on this agreement, the Army, in consultation with its auditors, will

- 1 develop a framework for conducting cost-benefit analysis for use in determining whether the consumption method is cost beneficial for selected instances of OM&S;
2. work with its auditors in developing specific criteria for determining when OM&S amounts are not significant for the purpose of using the consumption method;
- 3 develop functional requirements for feeder systems to support the consumption method; and
- 4 identify feeder systems that are used to manage OM&S items and develop plans to revise those systems to support the consumption method

Other Disclosures Needed

Adjustments and Devaluations. The Army logistics system, the Commodity Command Standard System, reflected \$46.7 billion in ammunition that the Operations Support Command managed and \$12.4 billion in munitions (conventional ammunition and missiles) that the Army Aviation and Missile Command managed, for a total of \$59.1 billion for munitions on hand. Several adjustments, totaling about \$40 billion, were made to the \$59.1 billion figure to obtain the value of the Army ammunition reflected on its financial statements.

- A reduction adjustment of \$31.6 billion was made to reflect the excess, obsolete, and unserviceable condition of ammunition on hand.
- A reduction of about \$12.4 billion was necessary because the material was identified in the logistics system as missiles, which are to be reported as stewardship property, plant, and equipment. Of the \$12.4 billion, \$8.4 billion was guided missiles and related equipment to be reported as property, but the remaining \$4 billion was ammunition.

-
- An addition of \$4 billion in material had been misidentified in a logistics system as missiles, as noted in the previously mentioned adjustment, but was really ammunition.

The Army did not reflect the adjustments to the \$59.1 billion anywhere on the financial statements. The \$40 billion value of adjustments exceeded the \$18.9 billion of ammunition reported. The adjustments are material and should be reflected on the financial statements. Also, because \$31.6 billion in adjustments represented a significant reduction in the value of Government assets, the Army should note and discuss the devaluation in the footnotes to the financial statements.

Overseas Ammunition. As part of the \$17.9 billion of OM&S held in reserve for future use, the Army reported about \$5 billion of ammunition not intended for use by U.S. forces. The ammunition was stored at depots overseas, generally not on installations occupied by U.S. forces. Although the Army had ownership of and title to the ammunition, the Army lacked the requirements, possession, and full stewardship for it. With rare exception, the ammunition was excess or obsolete to U.S. requirements. Under treaty agreements, the ammunition was not intended for use by U.S. forces, but was intended for use in defense of the host nation by the host nation. The host nation usually stored, guarded, and maintained the ammunition at its cost. If U.S. forces were to use the ammunition, the U.S. would be responsible for reimbursing the host nation for the storage and maintenance costs.

We believe that the \$5 billion of ammunition should be reflected on the financial statements. However, including it as held in reserve for future use overstates the assets of the Army. The reader of the financial statement could conclude that the \$5 billion was for U.S. forces' use. The \$5 billion in ammunition intended for others' use should be removed from "Held in Reserve for Future Use" and reflected elsewhere, such as under Footnote 8 B 2, "Restrictions on Operating Material and Supplies." That reflection would more realistically present the situation and provide more useful information to the reader.

Chemicals. The Army had substantial quantities of chemical munitions that were not reflected in OM&S. The Army stored about 26,200 tons of chemical munitions. The Army did not place a value on that stock. Because most of the stock was manufactured from the pre-World War II through Korean War time frame, the acquisition cost was relatively meaningless in today's terms. Also, international treaties prohibit the use of those munitions. As a result of the treaties, the Army is in the process of destroying the stocks at a cost of about \$16 billion. The existence of those stocks should be reflected under "Restrictions on Operating Materials and Supplies." The information would provide full disclosure, and the financial statements would be more useful to managers and other readers.

Recommendations

We recommend that the Assistant Secretary of the Army (Financial Management and Comptroller):

- 1. Reflect material adjustments for pricing errors and devaluation of excess, obsolete, and unserviceable ammunition in the financial statements, and disclose in the footnotes to operating materials and supplies the values of the adjustments.**

Management Comments. The Deputy Assistant Secretary of the Army (Financial Operations) nonconcurred and stated that the audit did not establish a basis for the recommendation. The \$40 billion of adjustments, referred to in the report, was not determined based on review of the Army financial statements, but from a review of information that Rock Island provided. If additional audit work is performed on financial statement information, and the need for corrective actions is established, the Army will reevaluate its nonconcurrence and take corrective actions where appropriate.

Audit Response. The Deputy Assistant Secretary's comments are nonresponsive. The ammunition data presented in the Army financial statements were derived from logistics systems, but they were adjusted, and the amount presented represents ammunition values on hand after \$40 billion in adjustments were made to the data. Financial statements inform decisionmakers in the Department, and Congress, about the value of the assets that DoD has available. Readers of the financial statements should be informed that \$31.6 billion of excess, obsolete, and unserviceable ammunition is on-hand and reported in logistics systems but not included in the amounts presented in the financial statements. Also, the Army should disclose that \$8.4 billion of missiles reported in the logistics systems as ammunition are reported as stewardship assets on the financial statements and that the logistics systems classify \$4 billion of ammunition as missiles. Footnote disclosure of the information is appropriate and essential to explain the difference between the amounts appearing in the financial statements and the amounts shown in the logistics systems. The adjustments are material, and presentation of the reasons for the adjustments of that magnitude would provide useful data to readers of the statements. The disclosure of the information would also reconcile the sizeable differences between amounts reported in the financial statements and the amounts shown in the logistics system. We request that the Army reconsider its position and provide comments on this recommendation in response to the final report.

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2. Remove from "Held in Reserve for Future Use" the \$5 billion of ammunition that the Army owned, but that is not intended for Army use, and reflect the amount under Footnote 8 B 2, "Restrictions on Operating Materials and Supplies," with an appropriate explanation.

Management Comments. The Deputy Assistant Secretary of the Army (Financial Operations) nonconcurrent and stated that Statement of Federal Financial Accounting Standards No. 3, October 27, 1993, paragraph 17, requires financial statement reporting when an activity has *title* to an asset. The removal of \$5 billion in ammunition from the Army balance sheet would cause the Army to underreport its assets by a material amount. However, he agreed that the usage restrictions on the ammunition are material and should be reported. He stated that he would expand the financial statements' notes to include an explanation on usage restrictions for the ammunition.

Audit Response. We consider the proposed action, to expand Army financial statements' notes to include an explanation on usage restrictions of ammunition, responsive because it satisfies the intent of the recommendation.

3. Disclose in "Restrictions on Operating Materials and Supplies" the amount of chemical stocks held pending destruction.

Management Comments. The Deputy Assistant Secretary of the Army (Financial Operations) nonconcurrent and stated that U.S. chemical weapons are currently awaiting destruction. The Army, as the executive agent for DoD, is responsible for the administration and operation of the chemical weapons destruction program. Army management of the program is reported in the liability section of the Army financial statements as required by both the Federal Accounting Standards Advisory Board and the DoD Financial Management Regulation. Neither the Federal Accounting Standards Advisory Board nor the DoD Financial Management Regulation requires the Army to continue to report or refer to assets previously written off or the amount of chemical stocks awaiting destruction in the financial statements.

Audit Response. The Deputy Assistant Secretary's comments are nonresponsive. This report discusses the reduction of current value of the on-hand chemical stocks to zero, and that possession of the stock is considered a liability. The zero value is based upon international agreements. Otherwise, the material would be an active ammunition item and, as such, reportable as OM&S in the financial statements. The DoD spent significant resources acquiring the stock and spends resources annually to safeguard it. We believe that the reader of the statements should be informed of the existence and amount of the stock and should be able to discern, over time, the progress made by the Army in destroying it. No provision or specific requirement exists to disclose chemical munitions in the financial statements, other than the liability for disposal of them. However, the significance of the

existence of 26,200 tons of those stocks, with disposal costs of \$16 billion, merits reporting their existence in the footnotes about Army assets. We request that the Army reconsider its position and provide comments on this recommendation in response to the final report.

Appendix A. Audit Process

Scope and Methodology

We concentrated our audit effort on the Army financial reporting of conventional ammunition. We examined \$18.9 billion of financial information related to Army OM&S, all of which represented conventional ammunition, and which was summarized in the FY 1999 financial statements. We also reviewed related information in reports produced by the Army from its financial and logistics systems and from the Army Audit Agency.

We performed the audit by making inquiries of Army comptroller and logistics staffs to determine the processes and policies that the Army used to report OM&S. This financial-related audit of \$18.9 billion that the Army reported of OM&S was conducted from September 1999 through March 2000 in accordance with auditing standards issued by the Comptroller General of the United States, as implemented by the Inspector General, DoD. The results of this audit did not rely on computer-processed data.

Contacts During the Audit. We visited or contacted individuals or organizations within DoD and the Army. Further details are available on request.

DoD-Wide Corporate-Level Government Performance and Results Act Goals. In response to the GPRA, the Secretary of Defense annually establishes DoD-wide corporate-level goals, subordinate performance goals, and performance measures. This report pertains to the achievement of the following goal, subordinate performance goal, and performance measure:

- **FY 2001 DoD Corporate-Level Goal 2:** Prepare now for an uncertain future by pursuing a focused modernization effort that maintains U.S. qualitative superiority in key warfighting capabilities. Transform the force by exploiting the Revolution in Military Affairs, and reengineer the Department to achieve a 21st century infrastructure.
- **FY 2001 Subordinate Performance Goal 2.5:** Improve DoD financial and information management. (01-DoD-2.5)
- **FY 2001 Performance Measure 2.5.1:** Reduce the number of noncompliant accounting and finance systems (01-DoD-2.5.1.)
- **FY 2001 Performance Measure 2.5.2:** Achieve unqualified opinions on financial statements. (01-DoD-2.5.2.)

DoD Functional Area Reform Goals. Most major DoD functional areas have also established performance improvement reform objectives and goals. This report pertains to achievement of the following functional area objective and goal:

- **Financial Management Functional Area. Objective:** Strengthen internal controls. **Goal:** Improve compliance with the Federal Managers' Financial Integrity Act. (FM-5.3)

General Accounting Office High-Risk Area. The General Accounting Office has identified several high-risk areas in the Department of Defense. This report provides coverage of the financial management high-risk area.

Prior Coverage

The General Accounting Office and the Inspector General, DoD, have conducted multiple reviews related to financial statement issues. General Accounting Office reports may be accessed on the Internet at <http://www.gao.gov>. Inspector General, DoD, reports may be accessed on the Internet at <http://www.dodig.osd.mil/audit/reports>. Army Audit Agency reports may be accessed on the Internet at <http://www.aaa.army.mil>.

Appendix B. Report Distribution

Office of the Secretary of Defense

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Under Secretary of Defense (Comptroller)
Deputy Chief Financial Officer
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Department of the Army

Assistant Secretary of the Army (Financial Management and Comptroller)
Auditor General, Department of the Army
Commander, Army Materiel Command

Department of the Navy

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House Committee on Government Reform
House Subcommittee on Government Management, Information, and Technology,
Committee on Government Reform
House Subcommittee on National Security, Veterans Affairs, and International
Relations, Committee on Government Reform

Department of the Army Comments



REPLY TO
ATTENTION OF

DEPARTMENT OF THE ARMY
OFFICE OF THE ASSISTANT SECRETARY
FINANCIAL MANAGEMENT AND COMPTROLLER
100 ARMY PENTAGON
WASHINGTON DC 20310-0109

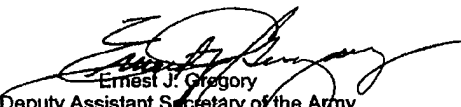
June 6, 2000

MEMORANDUM FOR DIRECTOR, FINANCE AND ACCOUNTING DIRECTORATE
INSPECTOR GENERAL, DEPARTMENT OF DEFENSE

SUBJECT: Audit Report on Army FY 1999 Financial Reporting of Conventional
Ammunition (Project No. D2000FJ-0069.001)

Reference your April 26, 2000 memorandum. We have reviewed your draft audit report on the Army's FY 1999 financial reporting of conventional ammunition in its financial statements. In addition, we have analyzed the report's recommendations and our responses and comments are attached.

My points of contact for this action are Mr. Donald Sketo, e-mail sketod@hdaa.army.mil, commercial (703) 697-6147 or DSN 227-6147 and Ms. Debra Rinderknecht, e-mail rinded@hdaa.army.mil commercial (703) 697-3971 or DSN 227-3971.


Ernest J. Gregory
Deputy Assistant Secretary of the Army
(Financial Operations)

Attachment

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**Army Comments on IG, DOD Draft Audit Report
"Army FY 1999 Financial Reporting of Conventional Ammunition"
Project No. D2000FJ-0069.001**

Recommendation 1. Reflect material adjustments for pricing errors and devaluation of excess, obsolete, and unserviceable ammunition in the financial statements, and disclose in the footnotes to operating materials and supplies the values of the adjustments.

NONCONCUR. The audit did not establish a basis for the recommendation. The \$40 billion of adjustments, referred to in the report, was not determined based on review of the Army's financial statements, but from a review of information provided by Rock Island. If additional audit work is performed on financial statement information, and the need for corrective actions to be taken is established, the Army will reevaluate its nonconcurrence and take corrective actions where appropriate.

Recommendation 2. Remove from "Held in Reserve for Future Use" the \$5 billion of ammunition that Army owned, but that is not intended for Army use, and reflect the amount under Footnote 8 B 2, "Restrictions on Operating Materials and Supplies," with an appropriate explanation.

NONCONCUR. Statement of Federal Financial Accounting Standards, Number 3, dated October 27, 1993, paragraph 17 requires financial statement reporting when an activity has title to an asset. The removal of \$5 billion in ammunition from the Army's balance sheet would cause Army to under report its assets by a material amount.

Army does concur that the usage restrictions on this ammunition are material to the financial statements and should be disclosed. Therefore, Army will expand its financial statements notes to include an explanation on usage restrictions for this ammunition.

Recommendation 3. Disclose in "Restrictions on Operating Materials and Supplies" the amount of chemical stocks held pending destruction.

NONCONCUR. U.S. chemical weapons are currently awaiting destruction. Army, as the executive agent for DoD, is responsible for the administration and operation of the chemical weapons destruction program for the U.S. Army management of this program is reported in the liability section of the Army's financial statements as required by both the FASAB and the DoD FMR. Neither the FASAB nor the DoD FMR requires the Army to continue to report or refer to assets previously written off or the amount of chemical stocks awaiting destruction in the financial statements.

Attachment

Audit Team Members

The Finance and Accounting Directorate, Office of the Assistant Inspector General for Auditing, DoD, prepared this report.

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